IN THE

Supreme Court of the United States

OCTOBER TERM 1945

No.

JULES E. PICCARD, on behalf of himself and for the benefit of and on behalf of the defendant, The Sperry Corporation, and all other stockholders of said defendant, The Sperry Corporation, who may be similarly situated,

Petitioner,

against

THE SPERRY CORPORATION, STANDARD CAPITAL COMPANY, J. CHEEVER COWDIN, THOMAS A. MORGAN, EDWARD ALLEN PIERCE, individually and as directors and voting trustees, etc., ALEXANDER B. ROYCE and JOHN SANDERSON, individually and as directors, etc., THOMAS B. DOE, individually and as officers, etc., and J. RUSSELL FORGAN, WRIGHT DURYEA and others, individually and as partners trading under the firm name and style of FIELD GLORE & COMPANY,

Respondents.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

POINT I

Field Glore should have been adjudged liable for participating with Cowdin in the breach of his trust and should have been charged with a positive duty to see to it, at its peril, that full and frank disclosure of all the facts was made to Sperry.

Cowdin's violations of his fiduciary duties to Sperry are established by the decision below (2615, 2632; Finding No. 26).

Field Glore knew that Cowdin was a director of Sperry and was acting for it as sole agent in connection with the sale of its Curtiss-Wright stock (456-457, 564, 655, 2637; Finding No. 34). In spite of this knowledge, Field Glore agreed to pay Cowdin's company, Standard Capital, fifty percent of its profits resulting from the option to purchase procured for it by Cowdin (450-456, 599, 1312).

Field Glore did realize that the arrangements should be fully disclosed to the Sperry directors (451), but the arrangements were not fully disclosed and, as the Courts below have found, the representation which Cowdin made to Sperry was untrue (2615).

We submit that Field Glore, if it wished to split its profits with Sperry's representative, was at the very least charged with the duty of seeing to it that Sperry was fully informed, not only that Cowdin's company was receiving a participation in its profits, but that it was receiving an unusual participation of as much as fifty percent.

The option which Field Glore thus obtained through Cowdin resulted in very substantial profits which were divided between Field Glore and Cowdin's company.

In *Cahall* v. *Lofland*, 12 Del. Ch. 299, 114 Atl. 224, one who had purchased property from a corporation, employed the president of the corporation as his agent to resell part of the property. The purchaser was held liable to the corporation for the profit resulting from the resale. The Delaware Court quoted with approval the following from *Panama* v. *Indian*, 10 L. R. Ch. App. Cas. 515:

> "But on such a subject as this, there shall not only have been an absence of concealment, but full and complete disclosure and information."

In *Jackson* v. *Smith*, 254 U. S. 586, at page 589, this Court said:

> "And others who knowingly join a fiduciary in such an enterprise likewise become jointly and severally liable with him for such profits."

To the same effect see:

Restatement of the Law of Restitution, Sec. 138 (2);
Irving Trust Company v. *Deutsch* (C. C. A. 2nd), 73 F. (2d) 121, certiorari denied, 294 U. S. 708;
Wechsler v. *Bowman,* 285 N. Y. 284;
Jacobellis v. *Prudential,* 244 App. Div. 255, 279 N. Y. Supp. 44, affirmed with modification on other grounds, 269 N. Y. 632;
Public Shoe Stores v. *Goldstein* (1st Dept.), 225 App. Div. 350, 233 N. Y. Supp. 73;
Mannaberg v. *Herbst,* 45 N. Y. Supp. (2d) 197, aff'd 267 App. Div. 818, 47 N. Y. Supp. (2d) 100, aff'd 293 N. Y. 657.

"We are told that the conflict of interest was sufficiently revealed when the brokers informed the plaintiff that the sale was to be made to a client of their office. Disclosure so indefinite and equivocal does not set the agent free to bargain for his own account or for the account of a corporation which acts through him alone. If dual interests are to be served, the disclosure to be effective must lay bare the truth, without ambiguity or reservation, in all its stark significance (*Dunne* v. *English,* L. R. 18 Eq. 524; *Imperial Merc. Credit Assn.* v. *Coleman,* L. R. 6 H. L. 189)." *Wendt* v. *Fischer,* 243 N. Y. 439, at p. 443.

Field Glore knew that its true arrangement with Cowdin was one which the Sperry directors, who were themselves fiduciaries, should not and could not approve.

In *Landes* v. *Hart* (1st Dept.), 131 N. Y. App. Div. 6, at page 7, 115 N. Y. Supp. 337, it is said:

"An agreement which is designed, or which in its nature and effect tends to lead persons who are charged with the performance of trusts or duties for the benefit of others to violate or betray them, is contrary to public policy and void and cannot be enforced. (*Bliss* v. *Matteson,* 52 Barb. 335, aff'd 45 N. Y. 22; *Moss* v. *Cohen,* 11 Misc. Rep. 184; *West* v. *Camden,* 135 U. S.

507; *Barkley* v. *Williams*, 26 Ill. App. 213.) Such a contract with a third person is not made valid although the acts of the unfaithful agent may have in fact resulted in benefit to his principal (*Lum* v. *McEwen*, 56 Minn. 278); *nor by the fact that the unfaithful director of a corporation informed his codirectors of his corrupt bargain.* (Munson v. S. G. & C. R. R. Co., 103 N. Y. 59, 74.)" (Italics supplied.)

See, also:

Hubbard v. *New York, N. E. & W. Investment Co.* (C. C. Mass.), 14 Fed. 675, aff'd 119 U. S. 696;

Keenan v. *Eshleman*, 23 Del. Ch. 234, 2 Atl. (2d) 904.

POINT II

The Courts below have erroneously held that there was no fiduciary relationship between Field Glore and Sperry; whereas Field Glore was in a fiduciary relationship to Sperry and is liable for the breach of its fiduciary obligations.

It was held below as a matter of law that there was no fiduciary relationship between Field Glore and Sperry (2663; Conclusion of Law 6).

At the suggestion of Cowdin, Sperry gave Field Glore, as stock brokers, an order to sell 90,000 shares of A stock at $10 a share (776-782, 1251-1252, 2209-2214; Exs. 1, 2). As stock brokers under this selling order, Field Glore were fiduciaries of their customer and principal, Sperry.

See:

McMann v. *Securities & Exchange Commission* (C. C. A. 2nd), 87 F. (2d) 377, 378;

Johnson v. *Winslow*, 155 Misc. 170, 279 N. Y. Supp. 147, aff'd without opinion 246 App. Div. 800, 285 N. Y. Supp. 1075, aff'd without opinion 272 N. Y. 476;

Taussig v. *Hart*, 49 N. Y. 301 and same case 58 N. Y. 425;
Conkey v. *Bond*, 36 N. Y. 427.

Field Glore immediately began through Cowdin to attempt to change its selling order as broker into an option to itself to purchase (636-637, 646, 656) and finally succeeded (445-448, 1291, 2225-2238; Exhibit 6, 2327-2330). As a fiduciary, Field Glore owed to its principal, Sperry, unequivocal and full disclosure that Sperry's representative in the negotiations, Cowdin, was to receive fifty percent of the profits resulting from changing that selling order into an option.

See:

Comments a and f to Section 390 of the *Restatement of the Law of Agency;*
Brown v. *Post*, 1 Hun 303, aff'd on opinion below 62 N. Y. 651;
Moffat v. *Gerry Estates, Inc.* (1st Dept.), 259 App. Div. 403, 19 N. Y. Supp. (2d) 579;
Franklin v. *Mortgage Guaranty & Security Co.* (C. C. A. 9th Cir.), 57 Fed. (2d) 834, at p. 835;
Anglo Eastern Trading Co., Inc. v. *New Tread Tire Company* (1st Dept.), 222 App. Div. 475, at p. 477, 226 N. Y. Supp. 532, at p. 534;
U. S. Ship Bd. E. F. Corp. v. *South Atlantic Dry Dock Co.* (C. C. A. 5th), 300 Fed. 56, at p. 61;
Wendt v. *Fischer*, 243 N. Y. 439, at p. 443;
Dunne v. *English*, L. R. 18 Eq. Cas. 524, at p. 533.

Thus, having realized very substantial profits in excess of ordinary brokerage commissions as a result of changing its selling order to an option, and in effecting such change having failed in its fiduciary obligation to make full and frank disclosure of Cowdin's participation, Field Glore is liable to account to Sperry for the resulting profits.

See:

Jackson v. *Smith*, 254 U. S. 586, at pp. 588 to 589;
Restatement of the Law of Restitution, Sec. 138;
Irving Trust Company v. *Deutsch* (C. C. A. 2nd), 73 F. (2d) 121, certiorari denied, 294 U. S. 708;
Wechsler v. *Bowman*, 285 N. Y. 284;
Wendt v. *Fischer*, 243 N. Y. 439;
Lonsdale v. *Speyer* (1st Dept.), 249 App. Div. 133, 291 N. Y. Supp. 495;
Jackson v. *Berry-Snelling Realty Co.*, 211 Ala. 174, 100 So. 111.

POINT III

The Courts below erred in holding valid under Delaware law the provision of Sperry's Charter purporting to authorize an interested director to be counted towards a quorum.

The certificate of incorporation of Sperry, a Delaware corporation, provides in paragraph "Tenth" thereof (2655-2656):

> "* * * Directors so interested may be counted when present at meetings of the Board of Directors or of such Committee for the purpose of determining the existence of a quorum.. Any director whose interest in any such contract or transaction arises solely by reason of the fact that he is a stockholder, officer or creditor of such company * * * shall not be deemed interested in such contract or other transaction * * *."

The learned Court below agreed that if the quoted provision is contrary to the laws of Delaware (whether statutory law or otherwise), it is invalid (2601-2602).

State ex rel. Cochran v. *Penn-Beaver Oil Co.*, 1926, 34 Del. 81, 143 Atl. 257.

The Court below held, however, that in the absence of what he considered a controlling Delaware authority, a Federal Court should not assume the provision to be contrary to Delaware law (2610-2611), and consequently that there were valid quorums at the June 30th, 1936, and July 28th, 1936, meetings which authorized and approved the settlement with Cowdin and Standard Capital. We submit that in this the Trial Judge erred.

The law is clear that the vote of an interested director may not be counted.

> *Keenan* v. *Eshleman*, 23 Del. Ch. 234, 2 Atl. (2d) 904;
> *Cahall* v. *Lofland*, 12 Del. Ch. 299, 114 Atl. 224;
> *Boray et al.* v. *H. M. Byllesby Co. et al.* (Sup. Ct., Del.), 38 Atl. (2d) 808;
> *Italo-Petroleum Corp.* v. *Hannigan*, 40 Del. 534, 14 Atl. (2d) 401.

In *Enright* v. *Heckscher* (C. C. A. 2d), 240 Fed. 863, it is said at page 872:

> "A director whose interest in a matter disqualifies him from voting upon a resolution concerning it cannot, according to the better opinion, be counted for the purpose of ascertaining whether a quorum is present when the vote is taken. A director so qualified by personal interest loses, pro hac vice, his character as a director and so cannot be counted."

That an interested director may not be counted towards a quorum is the universal rule. See cases cited in 14a *Corpus Juris* 1854 at page 92, and 19 C. J. S., Section 749 (c) at page 94, *all holding that an interested director is disqualified from being counted towards a quorum.* The District Court in its opinion (2605) cited two cases as holding contrary, *Gumaer* v. *Cripple Creek Tunnel T. & M. Co.*, 1907, 40 Colo. 1, 90 Pac. 81, and *Buell* v. *Buckingham*, 1864, 16 Iowa 284. *Gumaer* v. *Cripple Creek Tunnel T. & M. Co.* is no longer law in Colorado, in view of the later

decisions in that State, such as *Layburn* v. *Wrape*, 72 Colo. 339, 211 Pac. 367, and *Paxton* v. *Heron*, 41 Colo. 147, 92 Pac. 15. In the Iowa case cited by the District Court, *Buell* v. *Buckingham*, the by-laws provided that a quorum should consist of the president and two other directors. The question of the ineligibility of an interested president to be counted towards a quorum when present with two non-interested directors was not discussed by the Court and apparently was not raised. It was merely held that the affirmative vote of the two non-interested directors, constituting a majority of the quorum, was sufficient.

The above cited Delaware cases show that the Courts of that state have unequivocally declared that the vote of an interested director may not be counted. There was no reason for the Courts below to assume that Delaware would depart from what is now the universal rule and differentiate between not permitting a disinterested director to vote and not permitting him to be counted towards a quorum. Both are part of the same disqualification, the director having lost his character as a director, "*pro hac vice*", as pointed out by the Circuit Court of Appeals, Second Circuit, in the *Enright* case, *supra*.

The Courts below should have held the charter provision relied on by defendants a nullity and contrary to law, and that consequently the releases to Cowdin and Standard Capital Company were not valid corporate acts of The Sperry Corporation.

POINT IV

The Courts below erred in failing to ascertain the Delaware Law from all available data and to apply that law.

The District Court held that in the absence of what it considered to be controlling Delaware authority, it would not assume that the charter provision purporting to permit

interested directors to be counted towards a quorum was void as contrary to Delaware law. The Circuit Court of Appeals, Second Circuit, has sustained this holding. In the absence of a direct holding by the highest court in Delaware, it is the duty of the Federal Court to ascertain the law of Delaware "from all the available data" and apply it. This Court so held in *West* v. *American Telephone & Telegraph Co.*, 311 U. S. 223, at p. 237.

In *Fidelity Union Trust Co.* v. *Field*, 311 U. S. 169, at page 177, this Court stated:

> "* * * but it is still the duty of the federal courts, where the state law supplies the rule of decision, to ascertain and apply that law even though it has not been expounded by the highest court of the state. * * *"

As shown in the preceding point of this brief, all the avaliable data clearly indicates that the law of Delaware is the same as the law in other states, that an interested director may not be counted towards a quorum. Therefore, had the Courts below ascertained and applied that law they would have necessarily held that the charter provision relied upon by defendants was a nullity as being in conflict with the law of Delaware, the state of Sperry's incorporation, and that consequently the purported releases given to Cowdin and Standard Capital were not valid corporate acts.

POINT V

The decisions below constitute an impairment of the broad equitable principles which have been laid down by the Courts to govern fiduciaries, and sanction and establish a precedent by which such principles may be disintegrated, eroded, or evaded by subtle or narrow distinctions, and thereby injure public interest.

In *Meinhard* v. *Salmon*, 249 N. Y. 458, Judge Cardozo said, at page 464:

> "Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions (*Wendt* v. *Fischer*, 243 N. Y. 439, 444). Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court."

In 1934 the present Chief Justice of the United States wrote (48 Harv. Law Rev., p. 8):

> "I venture to assert that when the history of the financial era which has just drawn to a close comes to be written, most of its mistakes and its major faults will be ascribed to the failure to observe the fiduciary principle, the precept as old as holy writ, that 'a man cannot serve two masters'. More than a century ago, equity gave a hospitable reception to that principle, and the common law was not slow to follow in giving it recognition. * * * The separation of ownership from management, the development of the

corporate structure so as to vest in small groups control over the resources of great numbers of small and uninformed investors, make imperative a fresh and active devotion to that principle if the modern world of business is to perform its proper function. Yet, those who serve nominally as trustees, but relieved, by clever devices, from the obligation to protect those whose interests they purport to represent, corporate officers and directors who award to themselves huge bonuses from corporate funds without assent or even the knowledge of their stockholders * * * suggest how far we have ignored the necessary implications of that principle * * * but when we know and face the facts, we shall have to acknowledge that such departures from the fiduciary principle do not usually occur without the active assistance of some member of our profession * * *."

CONCLUSION

The petition for writ should be granted.

Respectfully submitted,

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